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Lampf v. Gilbertson: Rule 10b-5's Time Has Come

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LAMPF V. GILBERTSON: RULE 10b-5'S TIME HAS COME

I. INTRODUCTION

Individuals accused of violating Rule 10b-5, promulgated under the Securities Exchange Act of 1934 (1934 Act), have faced substantial uncertainty in determining the applicable statute of limitations.[1] Since 1946, circuit courts have looked to different provisions of state law to borrow limitation periods because section 10b of the 1934 Act does not articulate such a period.[2] These periods ranged from one to six years depending upon the state and source of the applicable limitation period.[3] In addition to states having different statute of limitations for the same action, courts have added to the confusion by borrowing limitation periods from different causes of action within each state. The area, therefore, lacked uniformity, predictability and a semblance of justice.

The United States Supreme Court recently provided a uniform, federal limitation period in *Lampf v. Gilbertson*.[4] The Court held the "one year from discovery, three years from the event" statute of limitations, derived from other sections of the 1934 Act, applied to all private Rule 10b-5 actions.[5] In doing so, the Court rejected the traditional practice of borrowing a statute of limitations from an analogous state cause of action. The majority also rejected an argument by the Securities and Exchange Commission (SEC) to adopt a five-year limit of repose from the recently enacted Insider Trading Act.[6]

This Comment will survey the Rule 10b-5 statute of limitation problem which gave rise to the *Lampf* decision. The Comment will provide a foundation to understanding the Court's decision through the Court's increasing practice of borrowing from federal analogies, and a review of

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1. Rule 10b-5, promulgated by the Securities and Exchange Commission reads:

> It shall be unlawful for any person, directly or indirectly, by use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
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> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5 (1991).

2. *See infra* notes 21-36 and accompanying text. For a discussion and breakdown of the limitation period applied by each Circuit, see James Beasley, *Committee on Federal Regulation of Securities Report of the Task Force on Statute of Limitations for Implied Actions*, 41 BUS. LAW. 645 (1986) [hereinafter "Task Force"].

3. *See* Roberts v. Magnetic Metals Co., 611 F.2d 450 (3d Cir. 1979) (applying New Jersey's six year statute for common law fraud); Fox v. Kane-Miller Corp., 542 F.2d 915 (4th Cir. 1976) (applying Maryland's one-year Blue Sky statute).

4. 111 S. Ct. 2773 (1991).

5. *Id.* at 2782.

6. 15 U.S.C. §§ 78t-1(a) and (b)(4) (1988).

the circuit courts' treatment of the problem. The Comment's analysis will focus on the ramifications of adopting the one-year/three-year limitation period and the Court's retroactive application of that decision.

II. BACKGROUND

A. *Traditional Statute Selection*

Statutes of limitations provide the judicial system with a means of limiting claims, which are impractical or inequitable to adjudicate due to the passage of time.[7] Generally, a legislature will either prescribe a limitation period for a newly enacted cause of action or simply apply a state's catchall statute. An implied cause of action, because of its very nature, has no prescribed limitation period.[8] Traditionally, federal courts have adopted a limitation period from an "analogous" state provision when no expressed limitation period is provided.[9] Since *Kardon v. National Gypsum Co.*, where a federal district court determined a private cause of action existed under Rule 10b-5,[10] the circuits have adopted limitation periods from a variety of state provisions.[11]

A court presiding over a Rule 10b-5 action faced a problem in determining which state-created cause of action was most analogous to the Rule 10b-5 claim.[12] The federal circuits found a variety of state actions

7. "[S]tatutes of limitation . . . protect the interests of three groups: potential defendants, the courts, and society in general. . . . A party does not have to defend itself after long periods of time, when evidence or witnesses may no longer be available." Neil Sobol, *Determining Limitations Periods For Actions Arising Under Federal Statutes*, 41 SW. L.J. 895, 897 (1987) [hereinafter Sobol]. "Temporal limitations, especially those of certain duration, assure potential defendants that they will not be forced to live indefinitely with the threat of a lawsuit." *See* Note, *Limitation Borrowing in Federal Courts*, 77 MICH. L. REV. 1127, 1128 (1979) (citations omitted) [hereinafter Note].

8. The adoption of a limitation period from an analogous state law is acceptable because "[w]hen Congress has not established a time limitation for a federal cause of action, the settled practice has been to adopt a local time limitation as federal law if it is not inconsistent with federal law or policy to do so." Wilson v. Garcia, 471 U.S. 261, 266-67 (1985). For a general discussion on the purpose of limiting actions, see Sobel, *supra* note 7.

9. Applying state limitation periods has been a time honored practice of the federal court system. *See* M'Cluny v. Sillman, 28 U.S. (3 Pet.) 270 (1830).

10. Kardon v. National Gypsum Co., 69 F. Supp. 512, 513 (E.D. Pa. 1946). The district court in *Kardon* based its decision that a private 10b-5 action existed on the common law approach that "[t]he disregard of the command of a statute is a wrongful act and a tort." *Id.*

11. *See* Bath v. Bushkin, 913 F.2d 817 (10th Cir. 1990) (applying limitation period for common law fraud); Smith v. Duff and Phelps, Inc., 891 F.2d 1567 (11th Cir. 1990) (applying limitation period from forum state's Blue Sky statute).

Blue Sky statutes are acts which regulate security transactions on a state level. The term "Blue Sky" originated in Kansas, which enacted the first effective securities statute. The statute and term are based on preventing promoters from promising only blue skies and rosy outcomes. *See generally*, LOUIS LOSS, FUNDAMENTALS OF SECURITIES REGULATION, 8 (1988) (hereinafter Loss).

Congress's numerous revisions of federal securities law have done little in providing further guidance, adding nothing concerning the private cause of action or an applicable statute of limitations for 10b-5 actions. Congress added the regulation of tender offers to the Act in 1968 and substantially broadened the regulation of the securities markets in 1975. *See generally*, *supra*, Loss, ch. 1.

12. "If Congress has not specified an applicable limitation period, the court must ex-

analogous. The First Circuit looked to personal tort actions.[13] Others focused on a state's Blue Sky limitation period.[14] Still others applied the state's common law fraud limitation period.[15] Some circuits, however, failed to consistently borrow the same state-created action from within each state, creating further inequities and confusion.

The circuits that adopted a state's fraud limitation period rationalized that Rule 10b-5 was enacted to facilitate prosecution of complex fraudulent securities transactions.[16] Securities laws, however, supplement, not supplant common law fraud actions. These circuits also emphasized that both actions have analogous proof requirements. Time constraints weighed heavily as another factor in favor of adopting a common law fraud limitation period. State legislatures generally provide a longer limitations period for fraud actions than for violations of securities laws. Courts viewed the extended period as being in line with Congress's intent of providing the aggrieved investor with an adequate remedy.

Several circuits applied limitation periods of a state's Blue Sky or securities statute. These also were troublesome, although they may initially appear most analogous to Rule 10b-5, as significant distinctions exist, including: (1) shorter limitation periods than those for common law fraud; (2) failure to encompass all of the relief available under Rule 10b-5 or the state's common law;[17] (3) failing to provide for equitable tolling to prevent an undiscovered claims from being time barred;[18] and (4) not requiring proof of scienter thus warranting a shorter limitation

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amine the nature of the cause of action to determine the time restriction." Holmberg v. Armbrecht, 327 U.S. 392, 395 (1946).

13. Maggio v. Gerard Freezer & Ice Co., 824 F.2d 123 (1st Cir. 1987) (applying a three-year limitation period and barring a thirteen-year-old action).

14. *Cf.* Smith v. Duff & Phelps, Inc., 891 F.2d 1567 (11th Cir. 1990) (rejecting federal analogy and applying Alabama's two-year limitation period); Herm v. Stafford, 663 F.2d 669 (6th Cir. 1981) (applying both a one-year securities limitation period and an amended three-year period to different 10b-5 claims); O'Hara v. Kovens, 625 F.2d 15 (4th Cir. 1980) (applying Maryland's securities tolling provision and one-year limitation period).

15. Nesbit v. McNeil, 896 F.2d 380 (9th Cir. 1990) (rejecting federal analogy and applying equitable tolling to Oregon's two-year fraud limitation period); Sioux Ltd. Sec. Litigation v. Coopers & Lybrand, 914 F.2d 61 (5th Cir. 1990) (applying Texas' newly enacted four-year fraud limitation period rather than two-year period in force at time of trial); Harris v. Union Elec. Co., 787 F.2d 355 (8th Cir. 1986) (applying Missouri's two-year fraud limitation period).

16. "The common-law fraud action was inadequate for the sophisticated transactions involving insider trading and market manipulation." Carlos J. Cuevas, *The Misappropriation Theory and Rule 10b-5: Deadlock in the Supreme Court*, 13 J. CORP. LAW 793, 795 (1988). "Thus, common-law actions in fraud or deceit failed to provide adequate protection for stockholders from individuals who traded on the market exchange based upon privileged access to corporate information. Due to the continued development of the impersonal market exchange, Congress sought to provide investor protection . . . ." Dana L. Hegarty, *Rule 10b-5 and the Evolution of Common-law Fraud-The Need for an Effective Statutory Proscription of Insider Trading by Outsiders*, 22 SUFFOLK U.L. REV. 813, 815 (1988).

17. *See* Biggans v. Bache Halsley Stuart Shields, Inc., 638 F.2d 605, 610 (3d Cir. 1980) (holding that where a Blue Sky statute does not provide the relief prayed for the statute of limitations from the common law action will prevail).

18. Aldrich v. McCulloch Properties, Inc., 627 F.2d 1036 (10th Cir. 1980).

period.[19] This last distinction presented problems as, in 1976, the United States Supreme Court held the scienter requirement applied to Rule 10b-5 actions.[20]

B. *The Rule 10b-5 Problem*

When a Rule 10b-5 claim accrues, the injured party must decide when and where to file a lawsuit. In the past, this has invited forum shopping because the statute of limitations applied to the particular action may have been longer in one jurisdiction than in another. Courts in Rule 10b-5 actions could do little to hinder this practice since the courts created the problem.

The disparity created by applying different limitation periods to Rule 10b-5 claims led both plaintiffs and defendants into a litigious mine field.[21] A Rule 10b-5 claim could be held time barred in one state or circuit and be found valid in another. This inequity in procedural process ran contrary to the universal belief that each individual should have the opportunity to play the game under the same set of rules.

The following two cases arising out of Pennsylvania in 1982 vividly illustrate the confusion in this area of law. In *Ging v. Parker-Hunter, Inc.*,[22] a group of investors brought an action under Rule 10b-5 alleging securities fraud. The securities dealer moved for summary judgment asserting that the claims were time barred under the Pennsylvania Securities Acts' ("PSA") two-year statute of limitations.[23] In addressing the limitations issue, the court focused on the remedy provided by the state statute rather than the elements of the offense. The court reasoned that the state fraud statute, not the PSA, provided investors with the remedy requested,[24] adopted the six-year limitation period for common law fraud, and held the claim was not time barred.[25] The PSA also differed from Rule 10b-5 by requiring privity.

In *Fickinger v. C.I. Planning Corp.*,[26] decided in 1982, six months after *Ging*, the plaintiffs brought a class action against a real estate investment trust, its advisor and the parent company. The plaintiffs maintained the statute of limitations for fraud applied. The court agreed, finding that common law fraud would be the only remedy provided under state law.[27] The defendant then argued that the two-year limitation period for fraud applied, while the plaintiffs contended that the six-year catch-

19. Diamond v. Lamotte, 709 F.2d 1419 (11th Cir. 1983); Biggins v. Bache Halsey Stuart Shields, Inc., 638 F.2d 605 (3d Cir. 1980).

20. Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976).

21. "A good illustration of the difficulties that can come up under either the passive or the active approach to borrowing state statutes of limitations is the problem of limitations for SEC Rule 10b-5 securities actions, presently one of the more confused areas of federal law." Sobol, *supra* note 7 at 1137.

22. 544 F. Supp. 49 (W.D. Pa. 1982).

23. 544 F. Supp. at 51.

24. *Id.*

25. *Id.*

26. 556 F. Supp. 434 (E.D. Pa. 1982).

27. *Id.* at 438.

all fraud limitation period was most appropriate.[28]

The Pennsylvania state legislature had enacted new statutes of limitation for a number of actions in the late 1970's.[29] The federal district court was forced to predict which limitation period was most appropriate because the Supreme Court of Pennsylvania had not yet decided the issue.[30] The court found the two-year period applicable but indicated that the jury was to determine when the plaintiffs had knowledge of the fraud and whether the limitation period had tolled.[31]

These cases illustrate the disparity and confusion created by the lack of a standard limitation period for Rule 10b-5 actions in a single state. Legislatively enacted statutes of limitation, on the state level, can change at the whim of the General Assembly and generally lack consistency with the purpose of the federal securities laws.[32] The problem became magnified when a circuit chose among different causes of action within each state,[33] or the parties involved in the action were within different circuits' jurisdiction.[34] Defendants and plaintiffs had no basis for determining whether a cause of action had tolled, thereby forstalling the suit. Federal securities actions became further complicated when the securities solicitation occurred telephonically because it raised complex choice of law questions.[35]

This disparity lead to inequities against defendants and may also have harmed unwary plaintiffs who inappropriately worded complaints by stating claims that would render the adoption of a shorter limitation period. Attempts by the circuits to impose some sense of certainty on Rule 10b-5 actions fell short of providing the uniformity necessary for an efficient and fair judicial system.[36]

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28. *Id.*

29. *Id.*

30. *Id.*

31. *Id.* at 440.

32. Within the Tenth Circuit the limitations period for fraud varies. Colorado, three years, *see* COLO. REV. STAT. § 13-80-101 (1989); Kansas, two years upon discovery, *see* KAN. STAT. ANN. § 60-513 (1983); New Mexico, four years, *see* N.M. STAT. ANN. § 37-1-4 (Michie 1990); Oklahoma, two years upon discovery, *see* OKLA. STAT. ANN. tit. 12 § 95 (West 1988); Utah, three years upon discovery, *see* UTAH CODE ANN. § 78-12-26 (1990); Wyoming, four years upon discovery, *see* WYO. STAT. § 1-3-105 (1988).

33. State legislatures are prolific in their adoption of statutes of limitations for varying causes of action. Colorado alone has well over twenty-five statutes of limitations ranging from COLO. REV. STAT. § 13-80-102, applying a two-year limitation period for claims under absolute liability to § 8-4-126, C.R.S., providing a two-year statute of limitations for wage disputes.

34. For a case dealing with a rule 10b-5 action with parties in different circuits, see Ceres Partners v. Gel Assocs., 918 F.2d 349 (2d Cir. 1990).

35. This is especially true with rule 10b-5 actions. The choice of law questions abound because of the preponderance of diversity citizenship suits; however, these are not within the scope of this Article.

36. *In re* Data Access Systems Securities Litigation, 843 F.2d 1537 (3d Cir.) (en banc), *cert. denied*, 488 U.S. 849 (1988); Ceres Partners v. Gel Assocs., 918 F.2d 349 (2d Cir. 1990) (applying an analogous federal statute of limitations); Short v. Belleville Shoe Mfg. Co., 908 F.2d 1385 (7th Cir. 1990) (applying an analogous federal statute of limitations), *cert. denied*, 111 S. Ct. 2887 (1991).

C. *Adoption of an Analogous Federal Limitation Period*

The Court has repeatedly stated that when Congress does not provide an express limitation period, it intends the adoption of a statute of limitations from a state-borrowed cause of action.[37] This principle is premised upon years of Court precedent and the Rules of Decision Act.[38] The state-borrowing doctrine may not be lightly abandoned because of congressional reliance. The Court has on a number of occasions, and particularly more recently, limited the choice of adoptable state actions, or simply adopted a limitation period from an analogous federal statute.

In *Del Costello v. International Brotherhood of Teamsters*,[39] the issue centered upon what limitation period would govern an employee's claim both against his employer for breach of a collective bargaining agreement and against his union for breach of duty of fair representation.[40] The claims were brought under different theories, including a contract claim against the employer and an arbitrator/bad faith claim against the union.[41] Recognizing the inherent inconsistency of both claims, the Court adopted the six-month limitation period prescribed under the National Labor Relations Act (NLRA).[42] In searching for an equitable limitation period, the Court found Maryland's one-year limitation period for breach of contract too long and thus inequitable to the defendant. The state's limitation period for vacating an arbitration award was considered too short to allow a plaintiff to reasonably assess the claim.[43] The Court determined the six-month period provided by the NLRA section 10(b) addressed the unique nature of employee/union disputes.[44] In citing prior decisions,[45] the Court found that Congress's specific intent was to balance national interests against individual rights when establishing the NLRA limitation period.[46] This balancing of interests, together with the intrinsic inconsistency of the claims, led to the rejection of a state-created analogy and the adoption of a federal statute's limitation period.

The Court has repeatedly stated that when a lower court chooses a statute of limitation, it should do so in a straightforward matter. In *Wilson v. Garcia*,[47] the Court determined the proper limitation period for bringing a Section 1983 civil rights claim. The majority recognized that

37. Wilson v. Garcia, 471 U.S. 261, 266-267 (1985); Campbell v. Haverhill, 155 U.S. 610, 617 (1895).

38. 28 U.S.C. § 52 (1990).

39. 462 U.S. 151 (1983).

40. *Id.* at 156.

41. *Id.* at 164.

42. 29 U.S.C. § 160(b) (1989).

43. 462 U.S. at 166.

44. *See id.* at 167-72. Six months would provide the employee with enough time to bring suit and also would be short enough to promote the federal policy of rapid final resolution of labor disputes.

45. *See* United Parcel Serv., Inc. v. Mitchell, 451 U.S. 56 (1981).

46. 462 U.S. at 171.

47. 471 U.S. 261 (1985).

a Section 1983 cause of action could be raised under differing legal theories, and a plaintiff could allege a number of different limitation periods.[48] The Court stated that Congress, in enacting the legislation, could not have intended such inconsistency in the enforcement of civil liberties.[49] The Court enumerated a three-part test for determining the most analogous state statute from which to borrow a limitation period. First, a court must decide whether state or federal law governs the characterization of the claim.[50] Second, if a federal characterization applies, the court must determine if all similar claims should be viewed in the same light or viewed differently depending on the circumstances.[51] Finally, the court must characterize the claim to establish which statute provides the "most appropriate limiting principle."[52]

In applying the test, the *Wilson* Court determined that Section 1983 provided "a uniquely federal remedy" against impediments of state law on civil liberties.[53] The majority reasoned that Section 1983 may "encompass numerous and diverse topics and subtopics" within each claim.[54] The Court acknowledged that while national uniformity in such actions was preferred, such consistency was not necessary,[55] and held that a Section 1983 limitation period must be consistently derived from the same state-based action within each state.[56]

In *Agency Holding, Corp. v. Malley-Duff & Associates, Inc.*,[57] the Court decided the appropriate limitations period for a private action brought under the Racketeer Influenced and Corrupt Organizations Act (RICO).[58] In *Agency*, an insurance agency alleged fraud and civil conspiracy three years after the alleged violative acts occurred. The district court held the claims were barred after applying a state-borrowed two-year fraud statute of limitations. The Third Circuit reversed, finding the state's six-year "catchall" statute the most appropriate. The Supreme Court, however, held a federal statute, the Clayton Act,[59] most analogous for adopting a statue of limitations.

In *Agency*, the majority found that a uniform federal limitation period better fulfills congressional intent because RICO claims embrace diverse local jurisprudential concepts. These legal concepts encompass "enterprise and pattern of racketeering activity" that do not conveniently fit into state-based common law statutory schemes.[60] The Court adopted the limitation period provided by the Clayton Act because both

48. *Id.* at 273-74.
49. *See id.* at 268-69.
50. *Id.* at 268.
51. *Id.*
52. *Id.*
53. *Id.* at 271-72.
54. *Id.* at 273.
55. *Id.* at 275.
56. *Id.* at 279. The statute of limitations for a personal injury was chosen as the appropriate limitation period for a Section 1983 cause of action arising in New Mexico.
57. 18 U.S.C. § 1961-68 (1989).
58. 483 U.S. 143 (1988).
59. 15 U.S.C. § 15(b), 18 U.S.C. § 1964.
60. 483 U.S. at 150.

the RICO and Clayton acts were structured to compensate for similar injuries and provide similar remedies.[61] Moreover, the possibility existed that a state's limitation period was too short.[62]

Del Costello and *Agency Holding, Inc.* hold that courts must adopt a federal limitation period when state limitation periods compromise congressional intent or fail to provide a reasonable time in which to bring an action. This determination must be made through an application of the three-part test enumerated in *Wilson*. The Court's repeated application and recognition of the state-borrowing method evidences a substantial presumption favoring state-borrowing.

The Supreme Court repeatedly denied certiorari in cases presenting a similar question as applied to Rule 10b-5.[63] Without guidance, a number of federal circuits began adopting limitation periods from analogous federal statutes in an effort to provide consistency to a prejudicial and chaotic situation.

D. *Rule 10b-5 and the Circuit Courts*

The increasing growth in the number of 10b-5 claims placed a significant burden on the federal courts. Rule 10b-5 was the federal securities regulation most often used by investors seeking remedy for a fraudulent act. The traditional state-borrowing method for selecting an appropriate limitation period proved burdensome, unpredictable and, quite often, inequitable. After almost forty years of adopting limitation periods ranging from one to ten years, several circuits began adopting a uniform circuit-wide limitation period.

In *In re Data Access Systems Securities Litigation*,[64] the Third Circuit, in an *en banc* decision, adopted a uniform, circuit-wide limitations period from an analogous federal securities statute. Prior to *Data Access*, the Third Circuit had applied a state's Blue Sky limitation period, unless that statute failed to provide the remedy sought by the plaintiff. In the latter instance, the court then would apply the limitation period of a state action most analogous to the claimed relief.

The *Data Access* plaintiffs argued for application of the New Jersey statute of limitations for common law fraud.[65] The Third Circuit rejected the common law fraud analysis, noting the lower threshold of proof needed in a Rule 10b-5 claim.[66] Rather than look to the usual alternative (the state Blue Sky statute), the court opted for a federal so-

61. *Id.* at 151.

62. *Id.* at 154.

63. *In re* Data Access Systems Securities Litigation, 843 F.2d 1537 (3d Cir.), *cert. denied*, 488 U.S. 849 (1988); Nortek, Inc. v. Alexander Grant and Company, 532 F.2d 1013 (5th Cir. 1976), *cert. denied*, 429 U.S. 1042 (1977).

64. 843 F.2d 1537 (3d Cir.) (en banc), *cert. denied*, 488 U.S. 849 (1988) (adopting limitation periods from the Securities Exchange Act of 1934, codified as amended at, 15 U.S.C. §§ 9(e), 18(c) and 29(b) (1988)).

65. *Id.* at 1538.

66. *Id.* at 1544.

lution. The Third Circuit concluded that language in *Del Costello*[67] and *Agency Holding*[68] authorized a retreat from the practice of state-borrowing.[69] In *Del Costello*, the Court adopted a limitation period from an analogous federal statute because state law provided an insufficient period. The *Agency Holding Corp.* decision rejected borrowing a state-created action because a common law action and RICO could not easily be compared or reconciled. In both decisions the Supreme Court, not finding a better analogous state source, adopted a limitation period from a federal statute.

The Third Circuit examined the problems arising out of the traditional practice of adopting state-borrowed limitation periods:[70]

> We are required to examine each contention of a federal securities complaint with great particularity to determine whether the state blue sky statute tracks the particular federal claim, and if not, to determine claim by claim which other state limitations period will apply depending upon the resemblance between the precise federal claim and those based in state or common law actions.[71]

The majority recognized that the traditional practice did not provide any "bright-line guidance" on the problem[72] and instead found that "[a] factual, claim-based approach to characterizing the case for limitations purposes would not promote [federal interests]."[73] The court reasoned that Congress intended to provide national and uniform remedies to fill a void in the common law. Using the analogy of the country as a "commercial universe," the court found state-based actions too diverse to accomplish the uniformity necessary to promote economic goals.[74]

In rejecting the adoption of a state action, the Third Circuit relied on Supreme Court dictum construing 10b-5 suits as not substantially analogous to fraud or deceit claims.[75] The majority found that section 10(b), companion sections 9(e), 18(c) and 29(b) of the 1934 Act and sections 12 and 13 of the 1933 Act accomplished the same objectives—provide full disclosure of the character of securities sold in interstate commerce and prevent fraud.[76] The court held these sections most analogous. With each section having a similar limitations period,[77] the court reasoned that "[w]hen Congress has created a right to sue in se-

67. 462 U.S. 151 (1983).
68. 483 U.S. 143 (1987).
69. 843 F.2d at 1540.
70. The court, in reexamining its Biggans v. Bache Halsey Stuart Shields, Inc., 638 F.2d 605 (3d Cir. 1980) decision, illustrates the problem arising out of a single 10b-5 claim of action within a single state and the disparity between the state's applicable statutes of limitation. 843 F.2d at 1541.
71. 843 F.2d at 1541.
72. *Id.*
73. *Id.* at 1543.
74. *Id.* at 1548-49.
75. 843 F.2d at 1545 (citing Basic, Inc. v. Levinson, 485 U.S. 224, 245 n.22 (1988)).
76. 843 F.2d at 1548.
77. *Id.*

curities matters, it has, with one exception, declared a limitations period no longer than three years."[78]

Following the *Data Access* decision, two other circuits adopted a similar approach. The Seventh Circuit adopted the one-year/three-year limitation period in *Short v. Belleville Shoe Manufacturing Co.*[79] After finding a uniform limitation period should apply to all Rule 10b-5 claims, the court focused on whether to adopt a limitation period from section 13 of the 1934 Act or the more recently enacted section 20A.[80] The majority concluded that section 13 had a more general application and was better suited for the wide variety of claims brought under Rule 10b-5. However, after reviewing a SEC amicus brief in a prior case,[81] the court found section 20A's five-year limitation period appealing. It reasoned the longer period may have been more reflective of Congress's most recent intent in enacting securities laws.[82] The five-year period of section 20A was rejected because of the prior adoption of section 13 by the Third Circuit and the court's paramount concern for national uniformity.

The Second Circuit, in *Ceres Partners v. GEL Associates*,[83] also adopted the one-year/three-year limitation period. The court relied heavily on *Data Access* because the plaintiff resided in the Third Circuit and the defendant in the Second. After considering section 20A, the court adopted the section 13 limitation period because of the great emphasis placed on the need for uniformity.

III. INSTANT CASE

With three circuits utilizing a single, uniform limitations period and all other circuits continuing the state-borrowing practice, the issue was ripe for United States Supreme Court treatment. The Court addressed the issue in *Lampf v. Gilbertson*.[84] In *Lampf*, the purchasers of shares in several failed limited partnerships brought suit against the law firm that prepared tax memoranda allegedly relied upon by the investors.[85] The investors claimed the law firm violated Rule 10b-5 by making misrepresentations that induced their investment. The district court granted summary judgment for the defendants, finding the claim barred by Oregon's two-year limitation period for fraud.[86]

78. *Id.* at 1550. Three judges dissented; however, the discussion focused on the majority's failure to address the question of retroactivity. The dissent found, after applying the three part test from *Chevron Oil Co.*, 404 U.S. 97 (1971), that the majority's holding should not apply to the case at hand. 843 F.2d at 1553.

79. 908 F.2d 1385 (7th Cir. 1990).

80. The statute of limitations for section 20(a) states: No action may be brought under this section more than five years after the date of the last transaction that is the subject of the violation. 15 U.S.C. § 78t-1(b)(4) (1990).

81. Brief for the United States, Lebman v. Aktiebolaget Electrolux, *cert. denied*, 109 S. Ct. 3214 (1989) (No. 88-1114).

82. 908 F.2d at 1391.

83. 918 F.2d 349 (2d Cir. 1990).

84. 111 S. Ct. 2773 (1991).

85. *Id.* at 2776.

86. *Id.* at 2777 (District Court decision is an unpublished opinion).

On review, the Ninth Circuit Court of Appeals reversed, finding that a question of material fact existed precluding summary judgment. In reversing, the court expressly rejected the defendant's claim that a federal limitation period should apply. The Supreme Court granted certiorari, citing the "divergence of opinion among the circuits regarding the proper limitations period."[87]

A. *Majority Opinion*

In adopting the one-year/three-year limitations period from the 1934 Act, the majority reiterated that a court's decision on the appropriate limitations period should be clear and straightforward.[88] Justice Blackmun, writing for the majority, enumerated a three-step, *Wilson*-like test for determining the appropriate limitation period when one is not expressly provided.[89] First, the court must determine the need for a uniform limitation period. When a federal cause of action can arise under different legal theories, the court should bow to predictability and judicial economy, and err on the side of uniformity.[90]

Second, the court should decide whether a state or federal source should provide the foundation for the limitation period. The majority specifically noted the geographic character of the claim as warranting additional consideration. When a claim can be multi-state in character, a federal limitations period is preferred to prevent forum shopping and to simplify the lower court's task.[91] Finally, any federal analogy must provide a "closer fit" to the litigated claim than is afforded by state borrowed sources.[92]

In applying this test, a need for a uniform limitation period for Rule 10(b)-5 claims was evident. The majority found that a national, uniform statute of limitations would both serve congressional intent and provide judicial economy. In assessing whether to look to a state or federal foundation, the Court rejected an assertion that state-based fraud statutes provided the closest analogy because Congress had expressly articulated several similar limitation periods in the same enactment.[93] These federal limitation periods recognize the expansive geographic character of Rule 10b-5 claims and shift the presumption to using a federal source. In rejecting the SEC's claim that a five-year statute of repose is more representative of congressional intent, the Court found that the express limitation periods from the 1934 Act provided the clearest evidence of such intentions at the time of enactment of section 10b.[94]

Finally, the majority rejected any application of the doctrine of eq-

87. *Id.*
88. *Id.* at 2779.
89. *Id.*
90. *Id.*
91. *Id.*
92. *Id.*
93. *Id.* at 2780.
94. *Id.* at 2780.

uitable estoppel to the new limitation period. It held the three-year component acted as a statute of repose, and application of the doctrine would be contradictory to the intent of the legislation.[95] The majority then found the investor's claims were time barred. In a terse concurrence, Justice Scalia articulated the need for congressional action and not judicial reaction.[96]

B. *Dissenting Opinion*

Justice Stevens, in a dissent joined by Justice Souter, echoed the concerns of Justice Scalia in recognizing the need for Congress to articulate limitation periods. In citing four decades of precedent and Congress's awareness of the state-borrowing doctrine, Justice Stevens argued that the Court had both made policy and possibly overstepped its constitutional bounds.[97] The dissent disagreed with the majority's reliance on *Agency Holding Corp.*, stating that RICO actions are relatively new and the adoption of a federal analogy (the Clayton Act) did not reverse forty years of precedent.[98]

Both Justices O'Connor and Kennedy authored concurring dissents. Justice O'Connor focused on the majority's retroactive application of the decision.[99] She observed that the claims were time barred because the plaintiffs were "unable to predict the future."[100] Citing *Chevron Oil Company v. Hulson*[101] as an example, Justice O'Connor stated that plaintiffs should be harmed for "sleeping on their rights," and not for relying on long established precedent.[102]

Relying on *Chevron Oil Company*, Justice O'Connor applied a three element test for determining whether a new decision may properly be applied retroactively. First, the decision must establish a new principle of law overriding clear past precedent relied on by the litigants.[103] Second, the Court must determine whether the retroactive application of a new decision will advance or retard the purpose and operation of the law.[104] Finally, the Court must establish that a retroactive application of its decision will not produce "substantial inequitable results."[105] In *Lampf*, the Court clearly disregarded the *Chevron* test. First, the Court overruled clearly established precedent. Second, while predictability is desirable in the future, it cannot be applied to the past. Finally, the majority's action was highly inequitable to the plaintiffs, who had litigated this issue for over four years.[106] Justice O'Connor believed that such

95. *Id.* at 2781.
96. *Id.* at 2783.
97. *Id.* at 2784 (Stevens, J., dissenting).
98. *Id.* at 2785.
99. *Id.* at 2785 (O'Connor, J., dissenting).
100. *Id.* at 2786.
101. 404 U.S. 97 (1971).
102. 111 S. Ct. at 2786.
103. 404 U.S. at 106.
104. *Id.* at 107.
105. *Id.*
106. 111 S. Ct. at 2787.

action by the majority went against earlier precedent, holding that application of a retroactive limitation period violates due process.[107]

Justice Kennedy's dissent focused on the three-year statute of repose adopted by the majority. Since Rule 10b-5 was aimed at fraudulent actions, he found the three-year period was contradictory to the intent of the rule.[108] Justice Kennedy reasoned that each "analogous" cause of action borrowed by the majority was fundamentally different from Rule 10b-5's anti-fraud character.[109] He recognized the limitation periods expressed in the 1934 Act may not be the most analogous to Rule 10b-5 claims.

This dissent noted the burden a plaintiff has in a fraud claim and that concealment is an inherent characteristic because of the very nature of fraud.[110] Noting that short statutes of repose are repugnant to fraud-based actions, Justice Kennedy believed that the majority's three-year repose period "simply tips the scale too far in favor of wrongdoers."[111]

IV. ANALYSIS

The Supreme Court's decision in *Lampf* evidences a common sense approach to a complicated statute of limitations problem. There are, however, areas in the majority's opinion that are inconsistent with precedent and demonstrate faulty logic. Specifically, the Court's actions evidence a trend rejecting the practice of state-borrowing and the federalization of certain common-law doctrines within the federal court system. The Court's cursory application of its own three-part test and the silent retroactive application of the decision go against the grain of justice and equity.

A. *Application of "Statute Selection" Test*

The majority's superficial application of its "statute selection" test to the Rule 10b-5 limitations problem produced the desired uniformity, but sacrificed law based upon thoroughly reasoned progressions. In choosing an appropriate limitations period in any particular Federal District or Circuit, it is abundantly clear that inconsistencies arise because of Rule 10b-5's diverse application. This broad application presents a cornucopia of legal theories and ancillary limitation periods to choose from because remedies for securities fraud can encompass tort or contract theories. The Court correctly determined that there was a need for a uniform statute of limitations for all 10b-5 actions, citing predictability and judicial economy as the main reasons.

Recognizing that a uniform limitation period can be applied on a state or national level, the majority next looked to the geographic character of the claim. Any survey of Rule 10b-5 claims clearly demonstrates

107. *Id.* at 2786.
108. *Id.* at 2790 (Kennedy, J., dissenting).
109. *Id.* at 2789.
110. *Id.*
111. *Id.* at 2790.

the complexity and geographic diversity of such causes of action. This was readily evident in *Ceres Partners*,[112] where the opposing parties resided in different circuits that utilized different limitation periods. The majority also recognized the threat of forum shopping and the general complexity of a Rule 10b-5 limitation ruling.

The analysis runs into trouble when the Court seeks a "closer fit" from a federal statute. It should be noted that the presumption rests on choosing a state-borrowed limitation period and that this presumption,[113] based on forty years of precedent, can only be overcome by a statute that is clearly more relevant and more properly tailored to the intent of Congress.

The Court concludes that other sections of the 1934 Act provide a "closer fit" for Rule 10b-5 actions because section 10(b) was enacted along with these other provisions.[114] The Court cites *Del Costello* as support for its assumption that a federal analogy is preferred.[115] The Court's reliance on *Del Costello* rests on a weak foundation. *Del Costello* dealt with claims that were commonly brought simultaneously between employee and employer, and employee and union, but under two distinct legal theories, including breach of contract and breach of duty.[116] In *Del Costello* the Court faced diversionary claims, which by their very nature gave rise to contradicting limitation periods when using the state-borrowing method. This inherent contradiction made it necessary for the Court to find a third, federal-based source for an equitable statute of limitations.

The *Lampf* Court's determination that the expressed limitations period provided in other sections of the 1934 Act is Congress's clearest intent is based on an assumption that the other sections remedy similar injustices and therefore related to section 10(b). This assumption is a long, logical leap because the majority does not point toward a particular statute section as it did in *Malley-Duff*.[117] There, the limitations period from the Clayton Act was applied to a RICO cause of action. The *Lampf* Court simply asserts that since the 1934 Act is directed, like Rule 10b-5, at securities improprieties, both statutory sections are clearly analogous.[118]

Justice Kennedy points out that these "analogous" sections articulate purposes other than those of Rule 10b-5. Section 78(i) prohibits acts of manipulation of security prices. The section specifically deals with misrepresentations of active trading, price fixing or violation of the rules and regulations of the Securities Commission. Section 78(g) prohibits misleading or false statements in general. These two sections deal

112. 918 F.2d 349 (2d Cir. 1990).
113. *Lampf*, 111 S. Ct. at 2778.
114. *Id.* at 2781.
115. *Id.* at 2780.
116. *Del Costello*, 462 U.S. at 164.
117. *Malley-Duff*, 483 U.S. at 150 (citing the Clayton Act, 38 Stat. 731, as amended, 15 U.S.C. § 15 (1990)).
118. *Lampf*, 111 S. Ct. at 2780-81.

with specific acts which, because of their narrow scope, may justifiably give rise to a one-year/three-year statute of limitations. Conversely, Rule 10b-5 and section 10(b) generally apply to any fraudulent securities transaction. The Supreme Court has held that under a 10b-5 claim a plaintiff must prove the elements of common law fraud, particularly scienter.[119] Additionally, Rule 10b-5's wide acceptance and use as a litigative tool provides evidence of its special status among securities law remedies available to an investor/plaintiff.

The very nature of fraud makes its discovery difficult. In contrast, it is substantively easier to trace a misleading statement or a price fixing scheme, particularly when a national securities trading board is involved in the monitoring and regulation of such transactions. It is clear that the Court's apparent acquiescence of the 1934 Act as a "closer fit" is built upon shaky ground. The Court states that the goal of securities laws is to protect investors against the manipulation of stock prices through regulation of securities transactions and exchanges. However, rule 10b-5 has been applied to a vastly wider scope of dealings, including sales of units in limited and general partnerships, activities not highly regulated.

Based on the Court's own presumption that state-borrowing is the appropriate method for selecting a statute of limitations when none is expressly provided, the Court failed to overcome that presumption and the Court's federal analogy should not stand. A good faith application of the Court's three-part test would have accorded the adoption of a longer limitation period. The five-year period enacted through the Insider Trading Act, as suggested by the SEC, would have provided continuity between each jurisdiction. Insider trading and fraud share common characteristics, such as difficulty of discovery. The five-year limitation period would both promote congressional intent and not undermine the principle use of Rule 10b-5, i.e., halting general securities fraud.

B. *Retroactivity*

The majority's decision to adopt a uniform, national statute of limitations for Rule 10b-5 actions is in accordance with virtually every commentator who has written on the subject. However, the Court's retroactive application of the limitation period is deplorable. As noted in Justice O'Connor's dissent, "the court shuts the courthouse door on respondents because they were unable to predict the future."[120] There can be very little "analysis" of the majority's retroactive application of the holding because the Court simply states that the plaintiff's actions are time barred.[121] No legal justification, based on case law or statute, is provided to support this ruling.

Such ruling by the Court goes against the grain of precedent, which consistently holds that when there is a drastic change in a well estab-

119. Ernst and Ernst v. Hochfelder, 425 U.S. 185 (1976).
120. 111 S. Ct. at 2786.
121. *Id.* at 2782.

lished law, especially a limitation period, it is inequitable to apply the new law retroactively.[122] In *Chevron Oil Company v. Huson*, the Court articulated a test for determining whether a judicial decision should be retroactively applied.[123] In *Chevron*, the Court was faced with a statute of limitations problem focusing particularly on a cause of action for personal injuries under the Outer Continental Shelf Lands Act. Congress had enacted a statute providing for federal rights and federal claims but failed to express a limitation period for such actions. The Court found that Louisiana's one-year statute of limitations for personal injury was the "closest fit." A retroactive application of the new limitation period would have barred the plaintiff's cause of action.

The Court articulated three separate factors for determining the retroactivity question.[124] These factors are: (1) whether there is established a new rule and overriding clear precedent; (2) whether retroactivity will retard the rule's purpose; and (3) whether retroactivity will produce "substantial inequitable results." In *Chevron*, the Court determined the statute of limitation should not be applied retroactively in that particular case. If the *Chevron* test is applied to the *Lampf* decision, it becomes clear that the new Rule 10b-5 statute of limitation should not be applied retroactively.

First, the Court's decision to apply the new limitations period to 10b-5 actions overrules clear precedent in the Ninth Circuit Court of Appeals, which, prior to *Lampf*, applied a limitation period by borrowing from the relevant state fraud claim.[125] Additionally, prior to the *Lampf* decision only three Circuits had determined that there was a clear federal analogy to 10b-5 actions. The first of these Circuits did not adopt the federal analogy rule until 1988. In fact it was only in the last three of Rule 10b-5's forty years of private use in civil litigation that the concept of federal analogy had even been adopted by the federal judiciary. It should be noted that the *Lampf* plaintiffs brought their action in 1986, two years prior to any Circuit's adoption of the federal analogy. It is readily apparent that the *Lampf* plaintiffs have fulfilled the first factor in the *Chevron* test. The Court overruled precedent on which the litigants had relied.

Second, in looking to the effect of this decision on Rule 10b-5, it is obvious that the application of a particular statute of limitations has a great effect on Rule 10b-5's use. Rule 10b-5 provides investors with a federal cause of action arising out of any fraudulent transaction dealing with securities. By applying such a short limitation period, the purpose of Rule 10b-5 will be greatly retarded. Now, as in *Lampf*, fraudulent actions must be discovered within three years. The retroactive application of the Court's decision on the *Lampf* plaintiffs is disastrous because the

122. *See* St. Francis College v. Al-Khazrhai, 481 U.S. 604, 608-09 (1987); *Chevron Oil Co.*, 404 U.S. at 97; Wilson v. Iseminger, 185 U.S. 55 (1902).

123. 404 U.S. at 106-07 (1971).

124. *See supra* note 101.

125. *Lampf*, 111 S. Ct. at 2785.

cause of action was not filed within the three-year statute of repose and therefore, the claims were barred. This is an onerous result after five years of litigation and reliance on well established precedent both in the Ninth Circuit and throughout the United States.

The third factor of the *Chevron* test, substantial inequity, is clearly met. The Court's determination to apply the new limitation period retroactively completely eliminated the plaintiffs' hopes for a successful litigative outcome and caused great injustice and substantial hardship which could have been avoided by not applying the decision retroactively. The Court's failure to follow *Chevron* in its decision not only harmed the plaintiffs but cast doubt on the Court's intellectual integrity. Aggrieved parties have no way of determining which precedent the Court will choose to apply or reject in any particular case.

V. CONCLUSION

No one argues with the Court's determination that claims brought under Rule 10b-5 are complex and diverse enough to warrant a uniform, national statue of limitations. The inequities placed on both the plaintiff and defendant are readily apparent through a reading of district or appellate opinions applying different statutes of limitations from different state-borrowed causes of actions. The majority's haste to bring order to this chaos has, however, missed an opportunity to make a well educated decision rather than a mere determination of law. The Court's adoption of the one-year/three-year statute of limitations from the 1934 Act may be judicially prudent but such a decision falls short of the Court's purpose. The Court, according to its own precedent, had a duty to find the "closest fit" for a Rule 10b-5 claim, not just the simplistic task of finding a justifiable alternative to the state-borrowing method. In rejecting the SEC's argument, which promoted the adoption of the five-year period of section 20(A), the Court failed to produce a uniform limitation period which would also advance Rule 10b-5's purpose of remedying fraudulent transactions. At the time of this writing, there is already a movement afoot in Congress to legislate a five-year statute of repose for Rule 10b-5.

While the Court's adoption of the one-year/three-year limitation may be defenseable, its retroactive application of this newly determined statute of limitations borders on a violation of a plaintiff's right to due process. To retroactively apply a law, after plaintiffs had spent an enormous amount of time and money relying on established precedent, went against all precepts of justice and equality. To apply the statute of limitations retroactively without a hint of justification or legal rationale is simply a slap in the face of any individual relying on any precedent, in any court. The injustice of the Court's retroactive application has far reaching ramifications. Lower courts will now retroactively apply the

new limitation period to bar unwitting plaintiffs.[126] The Court's decision merely to pass judgment and apply that ruling without any articulated reason diminishes respect for the Court and makes the legal community wonder whether, in the future, decisions will be founded on a rational extension of past precedent or merely the current whims of the judiciary.

Joseph Cachey III

126. *See* Lewis v. Hermann, No. 89 C 04576, 1991 WL 199627 (N.D. Ill. Sept. 17, 1991); Welch v. Cadre Capital, 923 F.2d 989 (2d Cir. 1991).